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IN THE

Supreme Court of the United States

October Term, 1956.

No. ~~1956~~ 130

FIDELITY-PHILADELPHIA TRUST COMPANY AND ROBERT B. HAINES, III, Executors of the Will of Mary H. Haines, Deceased,

Petitioners,

against

FRANCIS R. SMITH, Collector of Internal Revenue,

Respondent.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT.

ROBERT T. MCCRACKEN,
JOHN B. LEAKE,
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Philadelphia 2, Penna.,
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May 13, 1957.

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No.

FIDELITY-PHILADELPHIA TRUST COMPANY AND ROBERT B. HAINES, III, EXECUTORS OF THE WILL OF MARY H. HAINES, DECEASED,

Petitioners

against

FRANCIS R. SMITH, COLLECTOR OF INTERNAL REVENUE,

Respondent.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT.

To the Honorable the Chief Justice and the Associate Justices of the Supreme Court of the United States:

Petitioners pray that a writ of certiorari issue to review the judgment and decision of the United States Court of Appeals for the Third Circuit in the above case.

OPINIONS BELOW.

The opinion of the District Court (a copy of which is appended to this petition as Exhibit A) is reported at 142 F. Supp. 561.

The opinion of the Court of Appeals (a copy of which is appended to this petition as Exhibit B), reversing the District Court, is reported at 241 F. 2d 690.

JURISDICTION.

The judgment of the Court of Appeals (a copy of which is appended to this petition as Exhibit C) is dated February 28, 1957 and was entered on that date.

A petition for rehearing, filed with the Court of Appeals on March 11, 1957, was denied on March 15, 1957. A copy of the order of denial is appended to this petition as Exhibit D.

The jurisdiction of this Court is invoked under Title 28, United States Code, Sections 1254, 2101.

QUESTION PRESENTED.

The decedent, without medical examination, purchased three single premium life insurance policies and, as a condition of buying these policies, also purchased three single premium annuity contracts. She assigned the life insurance policies divesting herself of all interests in them. The assignees, who were also the beneficiaries, received the insurance proceeds on her death. The decedent retained the annuity contracts and received the annuity payments thereunder until her death.

The question is whether (1) the death proceeds of the life insurance policies or (2), in the alternative, their cash surrender values are includible in the decedent's gross estate, for estate tax purposes, under Section 811(c)(1)(B) of the Internal Revenue Code of 1939 as transfers in respect of which she retained the income for life or for a period not in fact ending before her death.

STATUTE AND REGULATIONS INVOLVED.

The statute involved is Section 811(c)(1)(B) of the Internal Revenue Code of 1939 and the regulations involved are Treasury Regulations 105, Section 81.18. The texts of the statute and regulations are set forth in the Appendix, *infra*.

STATEMENT OF THE CASE.

This is a suit by the executors under the will of Mary H. Haines, deceased, for refund of federal estate taxes (R. 3a-4a). The facts were stipulated (R. 3a) and may be summarized as follows:

The decedent in 1934 purchased three single premium insurance policies covering her life and also at the same times purchased three single premium non-refundable annuity contracts (R. 4a-5a). Each insurance policy was issued without medical examination on condition that the decedent purchase an annuity contract (R. 6a). She, however, could have purchased the identical annuity contracts at the prices she paid for them without buying the insurance (R. 5a). The separate premiums for each policy and contract were at the regular rates for a person of decedent's age (R. 5a, 11a-12a). The aggregate premiums paid for each insurance policy and annuity contract bought with it exceeded the face amount of the insurance, this being required by the issuing companies to protect themselves in the event the decedent died shortly after the purchase (R. 11a-12a).

During her life, the decedent assigned two of the life insurance policies to her children, giving them the right to exercise and enjoy every option, benefit, right and privilege conferred by the policies prior to their maturity (R. 6a-7a). This included, among other things, the right to surrender them and receive their cash surrender values, to change the beneficiaries, to borrow on the policies, and to receive dividends on them (Exhibits A and B, Stipulation of Facts; R. 6a-7a, 9a-10a). As to the third life insurance policy, the decedent assigned all options, benefits, rights and privileges prior to maturity to a trustee of a trust (R. 7a-8a). Like the first two policies, this included the right to cash it in, to borrow on it, and to receive dividends on it (Exhibits C, G and H, Stipulation of

Facts; R. 7a-8a). After July 6, 1938, the decedent had no beneficial or reversionary interest in the trust (R. 6a) and no reversionary interest in any of the three life policies (R. 6a, 8a). The decedent filed a gift tax return reporting as gifts the transfer of the three life insurance policies and paid gift tax thereon (R. 8a). If the assignees had surrendered the policies for their cash surrender values, this would not have affected at all the annuities the decedent was receiving, and continued to receive until her death, under the annuity contracts which she had retained (R. 6a). In so far as the record shows, if the assignees had cashed in the life insurance policies, there were no restrictions whatever on their use of any cash so received except that the trustee, as assignee of the one policy, would have held the cash it received subject to the trust (Exhibits G and H, Stipulation of Facts). The assignees did not surrender and cash in life insurance policies during the decedent's life (R. 11a).

In addition to being assignees of the two life insurance policies, the children were the named primary beneficiaries of all three such policies (R. 6a-7a). Thus, they received the full proceeds of all the life insurance upon the decedent's death in 1946 (R. 3a, 11a), to the exclusion of a trustee named by the decedent as a contingent beneficiary to take the share of any child dying before her (Exhibit C, Stipulation of Facts; R. 6a-7a). In summary form the assignees and named beneficiaries of the three life insurance policies were as follows:

		Named Beneficiaries	
	Assignees	Primary	Contingent
Two Life Insurance Policies	Decedent's children	Decedent's children	Trustee
Third Life Insurance Policy	Trustee	Decedent's children	Trustee

The executors did not include any of the value of the life insurance in the decedent's gross estate (R. 3a-4a). The Commissioner of Internal Revenue determined that the full insurance proceeds were includible and therefore asserted a deficiency in estate tax of about $97,000, which was paid (R. 3a-4a). Claim for refund was thereafter filed and disallowed (R. 4a). Petitioners then brought this suit in the District Court for refund (R. 4a), the jurisdiction of that Court being invoked under Title 28, United States Code, Section 1340, and Section 3772 of the Internal Revenue Code of 1939.

The District Court, Judge Kraft writing the opinion, considered the premiums paid for each life policy and the annuity contract bought with it to be an investment but one which was divisible and separable since the decedent had the right, which she exercised by the assignments, to separate the life insurance policies from the annuity contracts. It, therefore, following the decision of the Court of Appeals of the Seventh Circuit in *Bohnen v. Harrison*, 199 F. 2d 492 (1952), affirmed *per curiam* by this Court in a four-to-four decision, Justice Jackson not participating, 345 U. S. 946 (1953), rehearing denied 345 U. S. 978 (1953), held none of the insurance includible in the decedent's gross estate, since she had retained no income or other interest in the life policies—"in short, she retained no string over the proceeds of these policies" (R. 21a). The Court of Appeals reversed the decision of the District Court on the ground that, notwithstanding the assignments, the lifetime transfers of the insurance policies were essentially testamentary dispositions.

REASONS FOR GRANTING THE WRIT.

1. The decision of the Court of Appeals in this case is in direct conflict with the decision of the Court of Appeals for the Seventh Circuit in *Bohnen v. Harrison, supra.*

The factual situation in the *Bohnen* case, in its relevant details, is precisely the same as that here. Just like the

situation here, that decedent procured a policy of life insurance without medical examination for a single premium, and in connection therewith purchased for a separate single premium an annuity contract from the same insurance company. The life insurance policy would not have been issued to that decedent unless she had bought the annuity contract but she could have purchased the annuity without buying the insurance. Each decedent retained the annuity contracts and received the annuity payments thereunder until death but completely assigned the life policies divesting themselves of all interest in the life policies, reversionary or otherwise, and giving the assignees during the decedents' lives the right and privilege, among others, to change the beneficiaries, to borrow on the policies, to surrender them and obtain their cash surrender values. In each case the assignees, as the named beneficiaries, received the proceeds of the life policies on the decedents' deaths since they had not cashed in the policies. Had they cashed them in, the decedents' annuities would not have been affected in any way.

The *Bohnen* case involved the identical statute under the Internal Revenue Code of 1939 that is involved here. But the decision there was that none of the proceeds was includible in the decedent's gross estate, whereas the Court of Appeals in this case held the entire insurance proceeds includible. In the *Bohnen* case the Court of Appeals, like the District Court in this case, considered the insurance separable from the annuity contracts and premised its decision that the decedent had not transferred the insurance and still retained the income from it under Section 811(c)(1)(B) because of her lifetime assignment of all interest in the life insurance, stating (at p. 493):

> "* * * when the insured immediately transferred and assigned all of her right, title and interest of every character in and to the policy of insurance, that unit of her estate passed to the assignees, and was no longer

her property. It could, therefore, under no conception, constitute a part of her taxable estate when she died thereafter."

2. An important question of Federal law is involved here which has not been, but should be, settled by this Court.

For over fifteen years the problem of how to treat insurance in the circumstances presented here has vexed the Bar, the Bench, and the Treasury alike. The essential question in its barest form—still unanswered—is the same: Has a decedent retained the income for her life from property transferred by her and thereafter owned by the transferees although not reduced by them to possession? The precise issue presented here first arose in the Tax Court in 1941 in *Estate of Reynolds v. Commissioner*, 45 B. T. A. 44 and has since plagued the Courts of Appeal of the Second, Third, Sixth and Seventh Circuits, respectively, in *Estate of Burr et al. v. Commissioner*, 156 F. 2d 871 (C. A. 2, 1946), certiorari denied, 329 U. S. 785 (1946), this case, *Conway v. Glenn*, 193 F. 2d 965 (C. A. 6, 1952), and the *Bohnen* case.

Absent a decision by this Court, the uncertainty of the past will continue under the new tax laws, the Internal Revenue Code of 1954. The very same problem will arise under Section 2036(a) of the Internal Revenue Code of 1954, which is identical in all its relevant language to Section 811(c)(1)(B) of the 1939 Code. Nor will any other section of the 1954 Code provide the answer. The one dealing with transfers intended to take effect at or after death is not applicable unless a decedent retains a reversionary interest in the insurance. I. R. C. of 1954, Sec. 2037. Moreover, under the 1954 Code a decedent's payment of premiums will not, as was true here (Sec. 404(c), Rev. Act of 1942, 56 Stat. 945), cause the insurance proceeds to be includible in his gross estate. See I. R. C. of 1954, Sec. 2042.

The decision of the Court of Appeals in the *Bohnen* case presented for the first time a conflict in decisions between the different Courts of Appeal. This Court, recognizing the importance of this issue, granted certiorari in that case upon the Government's petition. Thus it has considered once before the precise question at stake here, but granting of the petition in this case will afford this Court the opportunity to decide the question left unanswered by its four-to-four decision in the *Bohnen* case.

In two other instances this Court also has rendered decisions on varying estate tax aspects of life insurance and annuity contracts purchased under circumstances like those here, yet neither of these decisions answers the question here. In *Helvering v. LeGierse*, 312 U. S. 531 (1941) Mrs. LeGierse bought an insurance policy and an annuity contract under circumstances like those here. She had not assigned the life insurance policy but owned it at her death. Hence, there was no issue such as here, and the basic question was whether her estate could benefit by the then statutory provision permitting an exclusion from the gross estate of $40,000 of life insurance. This Court denied the estate this exclusion on the ground that there was no real insurance at all, because of the absence of insurance risk. Essentially this Court found that the total consideration paid for both contracts represented one investment, but this Court also expressly recognized, in accordance with the facts, that this investment was divisible and separable, stating (at p. 541):

> "It is true that the 'insurance' contract looks like an insurance policy * * * and could have been assigned or surrendered without the annuity."

Also there was *Goldstone v. United States*, 325 U. S. 687 (1945) where an altogether different statute was involved. Because that decedent possessed at death a reversionary interest in the assigned life policy, this Court held the proceeds includible in his estate as a transfer intended to take effect at or after his death under Section

811(c)(1)(C) of the Internal Revenue Code of 1939. As in the *Bohnen* case that Section is inapplicable here because the decedent retained no reversionary interest in the transferred property. I.R.C. of 1939, Sec. 811(c)(2).

As evidenced by the many litigated cases, the purchase of insurance and annuity contracts in like situations has been common. The question here is also a live one today. The matter is one of importance, and there is no indication that it will be any less so in the future. The Solicitor General has acknowledged its continuing importance in his petition for certiorari in the *Bohnen* case, where it was stated (at p. 11):

> "The decision below raises an issue of continuing importance in the administration of the estate tax."

This frequently litigated question remains open and undecided. It should be settled.

3. The decision of the Court of Appeals below is clearly wrong and does not reach or answer the real issue in controversy.

Some of the language in the opinion of the Court of Appeals in this case is confusing and may be misleading. Therefore, that opinion will be briefly referred to. The opinion might lead to the belief that the assignees' right to cash in the life insurance policies was limited or that their use of any cash so obtained was not subject to present enjoyment. There is no warrant in the record for any such implication; under the assignments the assignees had the absolute right to cash in the life policies. The Government has conceded this to be so as stated in its brief before the Court of Appeals:

> "During her lifetime, the decedent assigned the life insurance policies, but the assignees neither borrowed on the policies nor exercised their privilege to take the cash surrender value." (Brief p. 3.)
>
> "Even though the decedent's children, or the trustee, in the case of the Hancock policy, had the right to

borrow on the life insurance policies and to obtain the entire cash surrender value, * * *." (Brief p. 16.)

The opinion of the Court of Appeals below might also lead one to believe that the instant case is distinguishable on its facts from the *Bohnen* case. Petitioners and the Government believe otherwise. At the hearing before the Court of Appeals, His Honor Judge Hastie asked a question to which Government Counsel, Mr. Rothschild, replied, the exchange being as follows:

"Judge Hastie: You agree that Burr and Bohnen and Conway are all indistinguishable from this case?

"Mr. Rothschild: That is our contention. And we agree that the Bohnen case is certainly indistinguishable in all material respects. If there are any differences they are not material for the purposes of this case."

Coming now to the statute, Section 811(c)(1)(B), according to its pertinent terms, will apply if a decedent makes a lifetime transfer of property and, quoting the statutory words in part, "he has retained" out of the transferred property the right to enjoy the income from it either for life, or for any period which does not in fact end before his death. The crux of this case is that these provisions are not satisfied at least with regard to that part of the investments represented by the cash surrender values of the life insurance policies, since before the decedent's death these separable and divisible amounts in their entirety, except for actual possession, belonged to the assignees. First, this is particularly clear with respect to the cash surrender values of the two life policies, which upon issuance were assigned to the children (R. 6a-7a). The decedent retained nothing whatever for any period of time from these cash surrender amounts. (After July 6, 1938, when she had completely assigned (R. 7a) the third life policy to the trustee, it is also clear that she had retained nothing from this policy). How in these circumstances could the decedent, having so given away these

amounts completely, be said at the same time to have retained something from them? Even if we assumed that the decedent derived some benefit from the cash surrender values being allowed by the assignees to remain in the hands of the insurance companies, though none is discernible, any such benefit would be a gift from the assignees and surely nothing she herself had retained or reserved, which the statute requires. The cases also show that the decedent himself must have done the retaining. *Estate of E. M. Uhl v. Commissioner*, 241 F. 2d 867 (C. A. 7, 1957); *Helvering v. Mercantile-Commerce Bank & Trust Company*, 111 F. 2d 224 (C. A. 8, 1940), certiorari denied, 310 U. S. 654 (1940); *Estate of Sessoms, et al. v. Commissioner*, 8 T. C. M. 1056 (1949). Second, with respect to the increases in the cash surrender values of the life policies taking place after the complete assignments of them, it is equally clear that the statute also is not satisfied. The simple reason again is that the assignees during the decedent's life, although not beginning with the assignment had, irrespective of her death, the one hundred percentum beneficial ownership of these amounts, including the right to all income therefrom and principal thereof. This is as true with respect to the amount of these increases just before her death as it is to such increases six months or a day before her death. In all such cases, it cannot be said that the decedent retained the income from these amounts for her life or for a period in fact ending with her death.

Apart from the above which constitutes the key to this case, the only interests the decedent retained—the annuity payments under the annuity contracts—did not, in any event, have their source in, and were not income from, that part of the investments represented by the cash surrender values, since these annuity payments would have continued precisely as before had the life policies been cashed in. Under the statute, only the property which is producing the income retained by the decedent is includible. Thus, also this requirement of the statute is not satisfied. Cash-

ing in the life policies, moreover, would have been altogether different from a sale by a remainderman of his remainder interest in a trust. In such circumstances, the entire trust corpus remains in the trustee's hands to throw off income for the life tenant, and neither the remainderman nor the new owner of the remainder interest can obtain permission from the trustee of the underlying trust properties until the trust ends. The opposite was true here.

The confusion in the cases, it is believed, has been caused by the failure of the courts to break down the aggregate investment (total premiums paid) into its separable parts, namely the cash surrender value which the assignees owned during the decedent's life and the excess over this amount which the assignees received on her death. Conceivably the decedent's death brought about an economic shift of this excess, but surely not with respect to (a) the cash surrender values of the life policies at the time of the complete assignments or (b) the higher cash surrender values just before the decedent died.

If the decision of the Court of Appeals in this case were allowed to stand, the statute would be sadly misconstrued. The fault would lie in the assignees' failure to reduce to possession that which they had every right to. Surely the mere reducing or not reducing to possession the cash surrender amounts cannot, in the light of the statutory language, be determinative.

CONCLUSION.

For the foregoing reasons this petition for a writ of certiorari should be granted.

Respectfully submitted,

ROBERT T. MCCRACKEN,
JOHN B. LEAKE,
Counsel for Petitioners.

Dated: May 13, 1957.

Appendix.

STATUTE AND REGULATIONS INVOLVED.

Internal Revenue Code of 1939.

SEC. 811. GROSS ESTATE.

The value of the gross estate of the decedent shall be determined by including the value at the time of his death of all property, real or personal, tangible or intangible, wherever situated, except real property situated outside of the United States—

* * *

(c) [as amended by Section 7(a) of the Act of October 25, 1949, c. 720, 63 Stat. 891] *Transfers in Contemplation of, or Taking Effect at, Death*—

(1) *General Rule.*—To the extent of any interest therein of which the decedent has at any time made a transfer (except in case of a bona fide sale for an adequate and full consideration in money or money's worth), by trust or otherwise—

* * *

(B) under which he has retained for his life or for any period not ascertainable without reference to his death or for any period which does not in fact end before his death (i) the possession or enjoyment of, or the right to the income from, the property, or (ii) the right, either alone or in conjunction with any person, to designate the persons who shall possess or enjoy the property or the income therefrom; or

* * *

(26 U. S. C. 1946 ed., Supp. III, Sec. 811.)

Treasury Regulations 105.

Sec. 81.18 [as amended by T. D. 5834, 1951-1 Cum. Bull. 72]. *Transfers with possession or enjoyment retained*—(a) *General Rule.*—Except in the case of a bona fide sale for an adequate and full consideration in money's worth, section 811(c)(1)(B) requires the inclusion in the gross estate of the value of all property transferred by the decedent, whether in trust or otherwise, if the decedent retained or reserved the use, possession, right to the income, or other enjoyment of the transferred property (1) for his life; or (2) for any period not ascertainable without reference to his death; or (3) for such a period as to evidence his intention that it should extend at least for the duration of his life and his death occurs before the expiration of such period. Except as provided in paragraph (b) of this section, such property is includible without regard to the date when the transfer was made, whether before or after the enactment of the Revenue Act of 1916.

* * *

(b) *Estate of decedents dying before January 1, 1950.* In the case of a decedent who died before January 1, 1950, property shall not be included in the gross estate under this section unless transferred—

(1) after March 3, 1931, and before June 7, 1932, and the retention or reservation by the decedent was (A) for his life or (B) for such a period as to evidence his intention that it should extend at least for the duration of his life, and his death occurs before the expiration of such period; or

(2) on or after June 7, 1932.

* * *

EXHIBIT A.

IN THE

UNITED STATES DISTRICT COURT

FOR THE EASTERN DISTRICT OF PENNSYLVANIA

CIVIL ACTION No. 14406.

FIDELITY-PHILADELPHIA TRUST COMPANY AND ROBERT B. HAINES, III, EXECUTORS OF THE WILL OF MARY H. HAINES,

Plaintiffs

v.

FRANCIS R. SMITH, COLLECTOR OF INTERNAL REVENUE,

Defendant

OPINION.

KRAFT, *J.* June 27th, 1956.

Plaintiffs seek to recover from the Collector of Internal Revenue a refund of estate tax deficiency assessed against and paid by the estate of Mary H. Haines, deceased, in the amount of $103,280.84 with interest. Detailed factual admissions, stipulations and findings are filed contemporaneously.

In April, 1934 Mrs. Haines, then aged 76, purchased a single premium life insurance policy in the amount of $200,000 for a premium of $179,358. On the same day she purchased from the same insurance company for a premium of $40,642 a non-refundable annuity contract which provided an annual payment of $5,026 to her for life, any balance on her death reverting to the company. In October, 1934 Mrs. Haines purchased from the same company another single premium life insurance policy in the amount

of $100,000 for a premium of $90,642. On the same day she also purchased from that company for a premium of $19,358 a non-refundable annuity contract which provided an annual payment of $2,440.64 to her for life, any balance at her death reverting to the company.

Both life insurance policies issued by this company designated as equal primary beneficiaries the four named children of Mrs. Haines and designated the Fidelity-Philadelphia Trust Company, as trustee under a trust agreement, as contingent beneficiary of the share of any of the children of Mrs. Haines who predeceased her. Pursuant to her written application for the policies each of these two life policies was issued designating her as the "Insured" and containing the provision noted in the margin.[1]

Later in October, 1934, Mrs. Haines purchased from a different company a third single life insurance policy in the amount of $50,000 for a premium of $43,491. On the same day she purchased from that company for a premium of $10,509 a non-refundable annuity contract which provided an annual payment of $1,295.56 to her for life, any balance at her death reverting to the company. Mrs. Haines' four children were named as beneficiaries of this life policy in which she reserved no right to change the beneficiaries; however, as issued, the policy proceeds were payable to her executors or administrators if her four children predeceased her. Thereafter, by assignment, Mrs.

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1. RIGHTS: Anything in this policy to the contrary notwithstanding, prior to the maturity of this policy, the Insured's children Isabella H. Miller, Margaret W. Haines, Robert B. Haines and Charles H. Haines jointly, the survivors or survivor, if none of said children be living, then the living children of said children of the Insured, jointly or the survivors or survivor, if none of the children of said children of the Insured be living, then to the executors or administrators of the last survivor of said children of the Insured and the children of said children of the Insured, some of the beneficiaries may, without the consent and to the exclusion of the Insured or any other beneficiary, receive, exercise, and enjoy every benefit, option, right and privilege conferred by this policy or allowed by the Company.

Haines included this life policy in a schedule forming part of the trust agreement between her and Fidelity-Philadelphia Trust Company and thereupon nominated that company, as trustee, to be contingent beneficiary of the policy which was amended so to provide on November 22, 1934. Under the terms of the trust agreement Mrs. Haines had reserved to herself all benefits, privileges and options available to her under this life policy including the rights of dividend receipt, assignment and surrender. She had reserved also the right to change, amend or revoke the trust agreement. On July 6, 1938 Mrs. Haines amended the trust agreement by assigning irrevocably to the trustee for the purposes of the trust all her right, title and interest in this and any other policy under the trust and by irrevocably empowering the trustee to exercise and enjoy all options, benefits, rights and privileges under this and other policies. By the same amendment she further provided that the trust agreement as so amended was thereafter unalterable and irrevocable. After July 6, 1938 neither Mrs. Haines nor her estate had any beneficial or reversionary interest in the trust or any reversionary interest in any of the three life policies.

In 1935 the four children filed appropriate returns reporting the receipt by each, as gifts from their mother, of a one-fourth interest in each of the life policies. In the same year Mrs. Haines suitably reported gifts of the three life policies to her children and paid gift taxes thereon.

The insurance companies required that the annuity contracts be purchased as a condition of issuance of the respective life policies. The annuity contracts and the annuity payments made to Mrs. Haines thereunder were not based upon or in any way dependent on the premiums paid by her for the respective life policies. The insurance companies would have issued these annuity contracts to Mrs. Haines or to any other person of her age for the same premiums without purchase of any life policies.

The deficiency assessment and the denial of the plaintiffs' refund claim were based on the contention that the life insurance policies were an investment rather than life insurance and that the value was taxable in decedent's gross estate under Section 811(c) of the Internal Code[2] either

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2. Sec. 811. Gross estate

The value of the gross estate of the decedent shall be determined by including the value at the time of his death of all property, real or personal, tangible or intangible, wherever situated, except real property situated outside of the United States—

(c) [as amended by Section 7(a) of the Act of October 25, 1949, c. 720, P. L. 378 (81st Cong.*)] transfers in contemplation of, or taking effect at, death:

* Section 7(b) of the Act of October 25, 1949 made this section as amended applicable to estates of decedents dying after February 10, 1939.

(1) General rule. To the extent of any interest therein of which the decedent has at any time made a transfer (except in case of a bona fide sale for an adequate and full consideration in money or money's worth), by trust or otherwise—

(A) in contemplation of his death, any transfer of a material part of his property in the nature of a final disposition or distribution thereof, made by the decedent within two years prior to his death without consideration, shall unless shown to the contrary, be deemed to have been made in contemplation of death within the meaning of this subchapter; or

(B) under which he has retained for his life or for any period not ascertainable without reference to his death or for any period which does not in fact end before his death (i) the possession or enjoyment of, or the right to the income from, the property, or (ii) the right, either alone or in conjunction with any person, to designate the persons who shall possess or enjoy the property or the income therefrom; or

(C) intended to take effect in possession or enjoyment at or after his death. . . .

(2) Transfers taking effect at death—transfers prior to October 8, 1949. An interest in property of which the decedent made a transfer, on or before October 7, 1949, intended to take effect in possession or enjoyment at or after his death shall not be included in his gross estate under paragraph (1) (C) of this subsection unless the decedent has retained a reversionary interest in the property, arising by the express terms of the instrument of transfer and not by operation of law, and the value of such reversionary interest immediately before the death of the decedent exceeds 5 per centum

as transfers intended to take effect in possession or enjoyment at or after death or as a transfer in decedent's lifetime of property, the right to income from which the decedent retained for life.

A transfer in which the transferor retains the income for life is quite different from a transfer intended to take effect in possession or enjoyment at or after death. Subsection (B) of Section 811(c)(1) of the Revenue Code of 1939 applies to the former and subsection (C) of that Section to the latter. The transfer by the present decedent

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of the value of such property. For the purposes of this paragraph, the term 'reversionary interest' includes a possibility that property transferred by the decedent (A) may return to him or his estate, or (B) may be subject to a power of disposition by him, but such term does not include a possibility that the income alone from such property may return to him or become subject to a power of disposition by him. The value of a reversionary interest immediately before the death of the decedent shall be determined (without regard to the fact of the decedent's death) by usual methods of valuation, including the use of tables of mortality and actuarial principles, pursuant to regulations prescribed by the Commissioner with the approval of the Secretary. In determining the value of a possibility that property may be subject to a power of disposition by the decedent, such possibility shall be valued as if it were a possibility that such property may return to the decedent or his estate.

Section 7(b) of Act of October 25, 1949, c. 720, P. L. 378 (81st Cong.)

(b) The amendment made by subsection (a) shall be applicable with respect to estates of decedents dying after February 10, 1939. The provisions of section 811(c) of the Internal Revenue Code, as amended by subsection (a), shall (except as otherwise specifically provided in such section or in the following sentence) apply to transfers made on, before or after February 26, 1926. The provisions of section 811(c)(1)(B) of such code shall not, in the case of a decedent dying prior to January 1, 1950, apply to—

(1) a transfer made prior to March 4, 1931; or

(2) a transfer made after March 3, 1931, and prior to June 7, 1932, unless the property transferred would have been includible in the decedent's gross estate by reason of the amendatory language of the joint resolution of March 3, 1931 (46 Stat. 1516). No interest shall be allowed or paid on any overpayment resulting from the application of subsection (a) with respect to any payment made prior to the date of the enactment of this Act.

occurred before October 7, 1949. Hence, even if Section 811(c)(1)(C) were applicable the inclusion of the value of the life insurance policies is barred by Section 811(c)(2) since the decedent retained no reversionary interest in the property transferred arising by the express terms of the instrument of transfer.

The defendant's earlier position, that the value of the three life policies were includible in the decedent's gross estate as transfers intended to take effect in possession or enjoyment at or after her death, appears to have been abandoned by the defendant in his brief and oral argument.

Determination of whether the value of the life policies are includible in decedent's estate as a transfer in her lifetime of property, the income or right to income from which she retained for life, involves a consideration of the applicability and rationale of the conflicting decisions upon which plaintiffs and defendant rely. Plaintiffs' prime dependence is upon Bohnen v. Harrison, 7 Cir., 199 F.2d 492.[3] Defendant is afforded support by Burr v. Commissioner of Internal Revenue, 2 Cir., 156 F.2d 871;[4] Conway v. Glenn, 6 Cir., 193 F.2d 965, and Estate of Reynolds v. Commissioner, 45 B.T.A. 44.

In the Burr case the decedent purchased three life policies and an annuity contract and irrevocably assigned the life policies to his children. The Court said:

> "The two purchases were obviously a single transaction, the annuity premium being part of the consideration for the insurance policies. Unless differentiated because of the subsequent assignment, therefore, the case is squarely within the Supreme Court's decision in Helvering v. Le Gierse, 312 U.S. 531, 61 S.Ct. 646, 85 L.Ed. 996, holding the proceeds of the policies taxable under § 811(c)."

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3. Affirmed per curiam by an equally divided court in 345 U. S. 946 (1953).

4. Cert. den. 329 U. S. 785 (1946).

With this construction of the Le Gierse case I am unable to agree. In Le Gierse, the life policy and annuity contract were similar to those in the instant case. However, that decedent had never assigned the life policy and still owned it at his death. It was payable to his daughter as beneficiary. His estate contended only that the policy proceeds were "insurance" and, being within the $40,000 exemption, were not includible in the estate. No contention appears to have been made by the estate in Le Gierse that the policy proceeds were not taxable as a transfer intended to take effect at death, if the proceeds were not "insurance." The basic question before the Supreme Court was whether the policy proceeds constituted an amount "receivable as insurance" within the meaning of § 302(g) of the Revenue Act of 1926. The Supreme Court held that, for purpose of determining whether the proceeds of the life policy were "insurance" within the meaning of § 302(g) the life insurance policy and the annuity contract must be read together, and that, so read, no essential element of risk existed and, hence, the proceeds were not true "insurance." The Supreme Court did not say that the two contracts were for all purposes indivisible or inseparable as the Burr and Conway v. Glenn cases decide. On the contrary the right of policy assignment was expressly recognized[5] in Le Gierse, but was deemed immaterial to the question of insurance risk then under consideration.

The Court's statement in Burr that the two purchases were a single transaction and that the annuity premium was part of the consideration for the insurance policies is true only in the sense that the insurance company would not have issued the life policies without the simultaneous purchase of the annuity. Unless the factual situation there presented differed from the present case or was misconstrued, it was erroneous to infer that the premiums for the life policies and the annuity contract were so commingled as to render the policies and the annuity one indivisible

5. 312 U. S. 531, 541.

asset. In the present case plaintiffs and defendant agree that no part of the premiums for the life policies paid for any annuity contracts and that the annuity premiums paid for no part of the life policies; further, that the present decedent or any other person her age could have purchased the same annuity contracts from the same companies for the same premiums without any life insurance.

The Court's conclusion in the Burr case that the decedent's transactions were an investment rather than insurance accords with the Le Gierse decision. That conclusion, however, does not justify the determination, unsupported by Le Gierse, that an investment so made is then and thereafter indivisible and inseparable.

The Burr case and Conway v. Glenn, supra, which followed it, gave scant attention to the import of Goldstone v. United States.[6] There the decedent had purchased and paid for a life insurance policy and annuity contract. As issued the life policy designated his wife as "Owner" and the decedent as the "Insured," and was payable on his death to his wife or, if she predeceased him, to their daughters. If all designated beneficiaries predeceased the decedent the policy proceeds were payable to his executors or administrators. The annuity contract, as issued, designated the wife as "Purchaser" and the decedent as "Annuitant." This contract provided for equal semi-annual payments to the decedent during his lifetime and for the payment of $6,071.46 to his wife upon his death or, if she predeceased him, to their daughters or, if they were dead, to his estate. Under both contracts the wife had the unrestricted power to assign, borrow, receive dividends, change beneficiaries and surrender. Both contracts provided that, if the wife predeceased the decedent, all of the enumerated powers were to vest in the decedent to the extent that such powers had not otherwise been exercised by the wife. The Court said:[7]

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6. 325 U. S. 687 (1945).
7. 325 U. S. at 690.

"*Helvering v. Le Gierse*, 312 U. S. 531, makes it plain that these two contracts, which must be considered together, contain none of the true elements of insurance risk. Section 302(g) of the Act, relating to amounts receivable 'as insurance under policies taken out by the decedent upon his own life,' is therefore inapplicable."

The Court then decided that the proceeds of the life policy and the balance of the annuity contract payable to the widow were includible in the decedent's gross estate under Section 302(c) as the subject of a transfer intended to take effect in possession or enjoyment at or after the decedent's death. The Court said:[8]

"The decedent, in making disposition of $25,000 of his property through these two contracts, retained a valuable interest in that amount which was not extinguished until he died. He retained not only the right to semi-annual payments under the annuity contract but also a contingent reversionary interest in the entire proceeds of both contracts. Had he survived his wife he could have exercised the attributes of ownership over the contracts, changing the beneficiaries or surrendering the contracts as he saw fit. If he had survived both his wife and his daughters the proceeds of the two contracts would automatically have been payable to his estate when he died. Thus the ultimate disposition of the proceeds of the contracts was suspended until the moment of decedent's death. Only then did the respective interests of the wife and daughters become fixed; only then were their interests freed from the contingency of the decedent's survival. His death was the decisive fact that terminated all of his potential rights, and insured the complete ripening of the wife's interests. . . . The string that the decedent retained over the proceeds of the contracts until the moment

8. 325 U. S. at 691-692.

of his death was no less real or significant because of the wife's unused power to sever it at any time.

The essential element in this case, therefore is the decedent's possession of a reversionary interest at the time of his death, delaying until then the determination of the ultimate possession or enjoyment of the property. The existence of such an interest constitutes an important incident of ownership sufficient by itself to support the imposition of the estate tax." (Emphasis supplied.)

While the specific question in the instant case was left undecided in Goldstone, it is clear that the decision did not give to Le Gierse the interpretation put upon the latter by the Burr case nor did it indicate indivisibility or inseparability. If, therefore, the present decedent had the right to separate the life insurance contracts from the annuity contract and to dispose of the former, she must be held to have done so conformably with the Goldstone decision since neither she nor her estate retained any direct or reversionary interest, contingent or otherwise, in the three life policies—in short, she retained no string over the proceeds of these policies after July 6, 1938.

That the life insurance policy is separable from the annuity contract under such circumstances as here exist was decided in a well-reasoned opinion in Bohnen v. Harrison in which the Court said:[9]

"Though the Supreme Court has decided that such an arrangement is in the nature of a single investment program and, therefore, not within the definition of insurance mentioned in the former act, $40,000 of which was then allowed to be deducted from the gross estate of a decedent, it does not follow that this investment program, made up of the two contracts, was indivisible. On the one hand, it is obvious that for the consideration

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9. 199 F. 2d at 493.

of some $22,000 a fixed annuity of $1600 was bought and that, on the other, in consideration of the sum of some $53,000 advanced, the company agreed to pay, at the insured's death a fixed sum of $72,000. The annuities were not based upon and in no wise dependent upon any consideration given for the life policy. The money to be paid under the life contract was in no wise based or dependent upon the sum advanced to secure the annuities. The two contracts constituted independent units, two pieces of property. Consequently, when the insured immediately transferred and assigned all of her right, title and interest of every character in and to the policy of insurance, that unit of her estate passed to the assignees, and was no longer her property. It could, therefore, under no conception, constitute a part of her taxable estate when she died thereafter."

The determination should rest upon the realities of the situation and the essential nature of the donee's ownership. The realities of the situation are that this decedent made investments which were not true insurance because no risk element to the insurer was involved. However, the life policies and annuity contracts were, on their faces, separate contracts and, while they must be read together to determine the realities, no valid reason is advanced by the defendant to hold that such an obligatory joint perusal welds them together permanently and indissolubly for all purposes.

Judgment will be entered in favor of the plaintiffs upon submission within fifteen days of an appropriate form of judgment.

C. William Kraft, Jr.,

J.

EXHIBIT B.

UNITED STATES COURT OF APPEALS
FOR THE THIRD CIRCUIT

No. 12,067

FIDELITY-PHILADELPHIA TRUST COMPANY AND ROBERT B. HAINES, III, EXECUTORS OF THE WILL OF MARY H. HAINES, DECEASED,

v.

FRANCIS R. SMITH, COLLECTOR OF INTERNAL REVENUE,
Appellant.

APPEAL FROM THE UNITED STATES DISTRICT COURT FOR THE EASTERN DISTRICT OF PENNSYLVANIA

Argued January 24, 1957

Before BIGGS, *Chief Judge*, and MCLAUGHLIN and HASTIE, *Circuit Judges.*

OPINION OF THE COURT

(Filed February 28, 1957)

By MCLAUGHLIN, *Circuit Judge.*

The question here is whether a death payment under a contract with a life insurance company is includible in the gross estate of the decedent under Section 811(c)(1)(B)

of the Internal Revenue Code of 1939, as amended, 26 U.S.C. 1952 ed. Sec. 811.[1]

In 1934, decedent, aged seventy-six, purchased three single premium insurance policies on her life. As a condition for the issuance of each policy the insurors required decedent to purchase an annuity in such amount that the sum of the premiums for death payment and annuity would equal approximately 11 10ths of the face amount of the death payment. In the policies decedent's four children were named primary beneficiaries and the Fidelity-Philadelphia Trust Co. (as trustee under a trust agreement) contingent beneficiary of the share of any of the decedent's children who predeceased her. In 1935, decedent reported on a gift tax return the interests transferred and paid the gift taxes thereon. By July 6, 1938, decedent had assigned irrevocably and unalterably to the beneficiaries all her

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1. Internal Revenue Code of 1939:

"Sec. 811. Gross Estate.

"The value of the gross estate of the decedent shall be determined by including the value at the time of his death of all property, real or personal, tangible or intangible, wherever situated, except real property situated outside of the United States—

* * *

"(c) [As amended by Sec. 7(a), Act of October 25, 1949, c. 720, 63 Stat. 891] Transfers in Contemplation of, or Taking Effect at, Death.—

"(1) General rule.—To the extent of any interest therein of which the decedent has at any time made a transfer (except in case of a bona fide sale for an adequate and full consideration in money or money's worth), by trust or otherwise—

* * *

"(B) under which he has retained for his life or for any period not ascertainable without reference to his death or for any period which does not in fact end before his death (i) the possession or enjoyment of, or the right to the income from, the property, or (ii) the right, either alone or in conjunction with any person, to designate the person who shall possess or enjoy the property or the income therefrom; or * * *"

rights in all death payments.[2] Until the date of death, decedent retained the annuity interests.

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2. As to the assignments of the three policies the findings are as follows:

"21. Pursuant to decedent's written application for the policies, each of the two life policies issued by The Mutual Life Insurance Company of New York contained at and after issue the following provision:

"RIGHTS: Anything in this policy to the contrary notwithstanding, prior to the maturity of this policy, the Insured's children Isabella H. Miller, Margaret W. Haines, Robert B. Haines and Charles H. Haines jointly, the survivors or survivor, if none of said children be living, then the living children of said children of the Insured, jointly or the survivors or survivor, if none of the children of said children of the Insured be living, then to the executors or administrators of the last survivor of said children of the Insured and the children of said children of the Insured, some of the beneficiaries may, without the consent and to the exclusion of the Insured or any other beneficiary, receive, exercise, and enjoy every benefit, option, right and privilege conferred by this policy or allowed by the Company.

"22. The decedent's four children were named as beneficiaries of the life insurance policy issued by John Hancock Mutual Life Insurance Company in which no right to change beneficiaries was reserved to the decedent. The policy, as issued, provided for the payment of the proceeds to the decedent's executors or administrators if her four children predeceased her. The decedent assigned this life policy to Fidelity-Philadelphia Trust Company, trustee, under a trust agreement between her and that company, and then nominated that company as trustee to be contingent beneficiary of this life policy, and on November 22, 1934 the policy was amended so to provide.

"23. Under the trust agreement decedent had reserved to herself all benefits, privileges and options available to her under the life insurance policy issued by John Hancock Mutual Life Insurance Company including rights of dividend receipt, assignment and surrender and had also reserved the right to change, amend or revoke the trust agreement. On July 6, 1938 the decedent amended the trust agreement by assigning, irrevocably to the trustee for trust purposes all her right, title and interest in this and any other policy subject to the trust agreement and by irrevocably empowering the trustee to exercise and enjoy all options, benefits, rights and privileges under this and any other policy subject to the trust agreement. By the same amendment the decedent further provided that the trust agreement as so

Decedent died May 7, 1946. In the estate tax return filed August 6, 1947, the death payments under the above contracts were not included in the gross estate. The Commissioner, under Sec. 811(c)(1)(B), assessed and collected a deficiency resulting from an audit which included those payments. After a claim for refund was disallowed, this suit was brought in the district court. The estate prevailed below and the government appealed.

Helvering v. LeGierse, 312 U. S. 531 (1941) removed the "life insurance" label from transactions such as these and directed that they be treated as investments. Goldstone v. United States, 325 U. S. 687 (1945), held the death payment in this type of transaction includible in the gross estate. Since then in United States v. Tonkin, 150 F. 2d 531 (3 Cir. 1945), cert. den. 326 U. S. 771, we held a similar death payment includible. The present situation is allegedly beyond the reach of those authorities as a result of the assignment of all the decedent's rights except the annuity to the trustee. That precise issue has been decided for the government in Reynolds v. Commissioner, 45 B.T.A. 44 (1941); Burr v. Commissioner, 156 F.2d 871 (2 Cir. 1946), cert. den. 329 U.S. 785; Conway v. Glenn, 193 F.2d 965 (6 Cir. 1952). The Court of Appeals for the Seventh Circuit did reach the opposite result in Bohnen v. Harrison, 199 F.2d 492 (7 Cir. 1952), Judge Duffy dissenting, affirmed by an equally divided court, 345 U.S. 946, rehearing denied, 345 U.S. 978. However, in a later opinion, Greene v. United States, 237 F.2d 848 (7 Cir. 1956), that court, construing the same section, 811(c)(1)(B), squarely conceded that "The decisive issue is whether, looking to substance and not merely to form, the decedent had retained for her life the right to the income from the property transferred."

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amended was thereafter unalterable and irrevocable. Neither decedent nor her estate had any beneficial or reversionary interest in the trust she created nor any reversionary interest in the life insurance policy issued by John Hancock Mutual Life Insurance Company after July 6, 1938."

The district court in following the Bohnen case misconstrues the Goldstone opinion. In the latter the court included the death payment in the gross estate on the ground that the decedent retained a contingent reversionary interest under Helvering v. Hallock, 309 U.S. 106 (1940), and found it unnecessary to reach the question whether the retention of the life annuity interest involved required its inclusion. There is nothing in Goldstone to support taxpayers' position.

It is urged that the annuity interests are completely separate and independent of the death payments and therefore cannot be encompassed by the following language of Sec. 811(c)(1)(B)—"* * * retained for his life * * * the right to income from the property * * * ". To demonstrate this independent taxpayers point to the fact that the annuity interests could be purchased by any one the age of the decedent for the same premium independent of the death payment. The illustration fails completely to show the independence of the death payment from the income payments for admittedly the death payment could not be bought without the income payments and it is the death payment which is sought to be included in the estate.

The argument itself exalts form over substance in an arrangement where the Supreme Court has specifically directed that the form be ignored. Helvering v. LeGierse, supra. The substance of the matter is that a capital fund—the premium—was deposited with the insurance company for a guaranteed annual return and repayment of the residue to beneficiaries on the death of the depositor. But for the insurance company's guarantee of the payments, it is identical to a transfer in trust with the settlor taking back a beneficial life interest. The assignments of all rights to the beneficiaries do not change the result. In the first place it does not appear that the beneficiaries received anything substantial since they were all contingent beneficiaries and survivorship was unknowable until the death of the decedent. While, theoretically, there may have been a pos-

sibility of anticipating the death payment by a cash surrender, the anticipators could do nothing with the cash until the survivorshop status was determined. A bare possibility of cash surrender does not change the inherently testamentary nature of this procedure. If a surrender is effected, a different problem is presented. Cf. Hutchinson v. Commissioner, 20 T.C. 749 (1953). Here the plain purpose was to convey the capital sum to the natural objects of the decedent's bounty in testamentary style and retain a life interest in the transferor. The small matter of the cash surrender right is well disposed of in Bank of New York v. Kelly, 135 N.J. Eq. 418 (1944) as follows:

> "In view of the conservative reason for the investment, it seems fantastic to suppose that a cancellation of the policy by Mrs. Parish during the lifetime of the insured at its surrender value was regarded by either as probable. If the decedent had intended to make a complete, absolute, and immediately effective gift, why would he resolve to invest a material portion of his estate in such manner that an enjoyment of it by the donee before his death would necessitate the loss incident to the surrender of the policy. Guggenheim v. Rasquin, 312 U.S. 254, 257. Cash or securities could well have been deposited in the trust instead of a single premium life insurance policy payable upon the event of death and having a surrender value based on a mortality table."

The district court was greatly impressed with the conclusion that the decedent had no ownership rights in the death payment after the assignments. In a sense, a life tenant has no ownership right in the remainder. But possession of legal title to the life policy after the assignment is not controlling. All of Section 811(c) is plainly directed at inter vivos transfers where title is no longer in the decedent at death. Taxation is a practical matter and the shifting of the economic benefits of the investment occa-

sioned by the death of the decedent is too much akin to a testamentary disposition not to be subjected to the same tax under Sec. 811(c)(1)(B). See Helvering v. Bullard, 303 U.S. 297 (1938).

The judgment of the district court will be reversed and the case remanded with the direction that judgment be entered in favor of the defendant (appellant in this court).

EXHIBIT C.

UNITED STATES COURT OF APPEALS
FOR THE THIRD CIRCUIT

No. 12,067

FIDELITY-PHILADELPHIA TRUST COMPANY AND ROBERT B. HAINES, 3D, EXECUTORS OF THE WILL OF MARY H. HAINES, DECEASED

v.

FRANCIS R. SMITH, COLLECTOR OF INTERNAL REVENUE, *Appellant*

ON APPEAL FROM THE UNITED STATES DISTRICT COURT FOR THE EASTERN DISTRICT OF PENNSYLVANIA

Present: BIGGS, *Chief Judge*, and MCLAUGHLIN and HASTIE, *Circuit Judges*.

JUDGMENT

This cause came on to be heard on the record from the United States District Court for the Eastern District of Pennsylvania and was argued by counsel.

On consideration whereof, it is now here ordered and adjudged by this Court that the judgment of the said District Court in this case be, and the same is hereby reversed, and the case remanded with direction that judgment be entered in favor of the defendant-appellant.

Attest:

IDA O. CRESKOFF,
Clerk.

February 28, 1957

EXHIBIT D.

UNITED STATES COURT OF APPEALS
FOR THE THIRD CIRCUIT

No. 12,067

FIDELITY-PHILADELPHIA TRUST COMPANY AND ROBERT B. HAINES, III, EXECUTORS OF THE WILL OF MARY H. HAINES, DECEASED

v.

FRANCIS R. SMITH, COLLECTOR OF INTERNAL REVENUE,
Appellant

SUR PETITION FOR REHEARING

Present: BIGGS, *Chief Judge*, and MCLAUGHLIN and HASTIE, *Circuit Judges*.

After due consideration the petition for rehearing in the above-entitled case is hereby denied.

BY THE COURT,

MCLAUGHLIN,
Circuit Judge.

Dated: March 15, 1957